GENERAL INVESTMENT CLIMATE

The Economy

The recovery that already became apparent from the spring onwards continued to manifest itself during the last quarter of 2009. The economic climate improved in all important economic regions.

In December, German producer confidence reached its highest level in seventeen months. Order books are filling up again, mainly thanks to the strong demand from Asia, that increasingly is becoming the motor of the world economy. In the US, the ISM-indicator of industrial activity reached its highest level for over three years, consumer confidence bounced back in December after a short fallback, and the housing market also seems to stabilize.

However, one should not forget that all in all, 2009 was a disastrous economic year; for the first time since World War Two, global economic activity decreased on an annual basis. While most emerging economies – with the noticeable exception of Russia and Eastern Europe – continued to grow, the developed countries were severely hit. The real GDP fell ca. 2.5% in the US over the full year 2009 and even 4% in the Eurozone. Japan also had to face a heavy recession.

Most economic institutions expect a slow and difficult recovery for 2010, burdened by the deep impact of the economic crisis on unemployment and budget deficits.

In the Eurozone, unemployment rose to 9.8% in October, an increase of 2.3 percentage points year-on-year. In the US, unemployment reached 10.0% in November, an increase of 3.2 percentage points y-o-y. However, this was 0.2 percentage point less than in October. The past week, the number of unemployment requests unexpectedly fell to the lowest level since July 2008, another sign that the US economy is improving.

In general, the American economy (once again) proves to be more resilient than the European. For 2010, the Federal Reserve expects a growth of 2.5-3.5%, meaning the US economy would be back at its pre-crisis size. In Europe it could take until 2012 before the damage is repaired. Not only was the decline steeper, the recovery will probably also be slower; most economists only expect a modest growth of 0.5-1% for Europe in 2010.

The big question remains how sustainable the recovery of the past months will turn out to be. A relapse cannot be excluded, as the recovery is mainly due to the strong demand from China (that will not be able to juggle with growth figures of 9-10% forever) on the one hand, and all kinds of temporary relaunch measures – monetary and fiscal stimuli, such as the cash for clunkers (CARS) program – on the other hand. Moreover, the positive restocking effects should start to evaporate in the second half of the year.

Governments will have to deal with limited room for manoeuvre the upcoming years, due to the derailed public finances. The private sector will thus gradually have to take over from the government. Because the mounting unemployment will continue to weigh on consumption for some time to come, the positive impulses will mainly have to come from the export and corporate investments.

After seven months, the Eurozone finally returned to inflation in November; the general price level rose 0.5% compared to October. For the full year 2009, inflation will be ca. 0.3%, for 2010 the ECB expects an inflation rate of 1.3%. This will largely depend on the evolution of the oil price, which nearly doubled over 2009, ending the year close to $80.

A technical reaction (i.e. the low comparative basis of oil prices at the start of 2009) should normally see inflation increasing the coming months.

Money markets and exchange rates

The interest rates of the main central banks remain anchored at extremely low levels since spring 2009. A tightening of monetary policy is not expected before the second half of 2010.

The unconventional measures that central banks have taken to tackle the economic crisis, such as the purchase of bonds and restructured loans, certainly contributed to the rather swift return to economic growth of most economies.

The question is which exit-strategy the central banks will pursue, and how the markets will react when these measures are reversed. The ECB was the first to announce that it will terminate its exceptional measures. By the end of 2010, there will be no additional lending facilities available any more.

On the interbank markets, the European 3-month interbank rate declined further, to finish the year at a low of 0.700%. The long-term rate in Europe recovered slightly, towards 3.555%. Consequently, we are currently witnessing the steepest interest rate curve since the introduction of the euro.

On the exchange markets, the euro initially strengthened further against the dollar, above the 1.50 USD mark, before falling back strongly in December, to end the year at 1.43 USD. This was mainly due to a rating downgrade for Greece (that carries a budget deficit of 12%) and the possibility of similar consequences for other member states such as Spain and Ireland.

Stock Markets

Table 1.1 - General

	31/dec/09	30/sep/09 - 3 mth	30/jun/09 - 6 mth	31/mrt/09 - 9 mth	31/dec/08 - 12 mth
AEX	335,33	7,70%	31,65%	54,54%	36,35%
BEL20	2511,62	1,05%	23,67%	43,62%	31,59%
DAX	5957,43	4,97%	23,89%	45,85%	23,85%
EU50	2964,96	3,21%	23,45%	43,16%	21,14%
DJ	10428,00	7,37%	23,45%	37,05%	18,82%
SP500	1115,10	5,49%	21,30%	39,76%	23,45%
Nasdaq	2269,15	6,91%	23,66%	48,45%	43,89%
EUR/USD	1,4326	-2,13%	2,09%	8,10%	2,53%
EUR 3 months	0,7000	-0,0530	-0,3990	-0,8100	-2,1920
EUR 10 year	3,5550	0,0440	-0,2440	-0,1830	0,0090

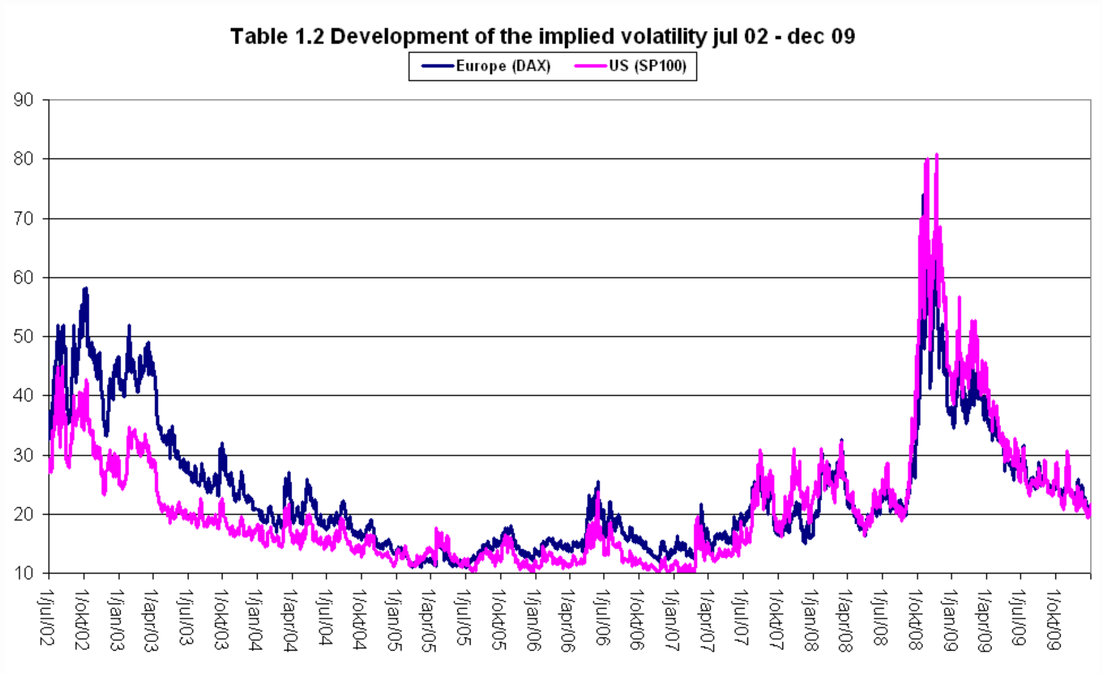
After a fairly strong final quarter, with gains of ca. 5%, the main stock markets ended 2009 near their highs of the year. On an annual basis, the gains amount from ca. 20% (Dow Jones, DAX, Eurostoxx 50) to over 30% (AEX, Bel20). The Nasdaq even rose by nearly 44%. Although most markets hereby realized their best performance of the past decennium, they only made up part of the losses of 2008, and are currently still 30-40% below the levels of end 2007. There certainly still is upside potential, the stock markets do not appear to be overvalued yet.

The small- and midcap indices performed less well than the main indices in the fourth

quarter, especially the MDAX (+2%) and the SDAX (+1.5%). The AMX (+7.5%) and the ASCX (+5%) were able to notch a nice gain.
However, on an annual basis the small- and midcap indices still performed better than the main indices: AMX + 64%, ASCX +45%, MDAX+34%, SDAX +27%.

Implied volatility

Stock market volatility decreased further over the past quarter, to a rather low level of ca. 20%.



Long-term development

The AEX was able to continue its positive trend of the previous quarters, ending the year at a level of 335.33, 68% above the lows of begin March. On an annual basis, the AEX gained over 36%.